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Building A Health Marketplace That Works

July 31st, 2009

by Alain C. Enthoven

In the debate about health reform, many issues are getting an inordinate amount of attention, but one is not getting the detailed consideration it deserves. How it is finally resolved is likely to be one of the key factors of the ultimate plan's success or failure. That issue is the design of the *health insurance exchange.*

An exchange is a managed marketplace in which individuals can choose among a variety of health plans. Why do we need an exchange? An exchange would help to remedy serious deficiencies in the current health care system:

• **Lack of consumer choice.** Most employees are offered only one insurance option. Health insurers usually don't allow small employers to offer competing plans, due to high administrative costs and concerns about adverse selection; as a result, the employer is forced to accept a "one-size-fits-all" plan for her/his employees. This is usually an expensive "fee-for-service" plan that rewards doctors for volume of services but not quality of care. The lack of choice for employees also means that there is no effective competition among insurers at the consumer level. This market blocks the growth of efficient integrated financing and delivery systems, which are not good candidates for the role of an employer's sole plan.

• **High costs.** Small employer groups and individuals pay higher premiums than larger groups for similar health benefit plans. This is due primarily to higher selling and administrative costs for insurers in the small-group and individual segments.

• **Unstable premiums**. Many employers are too small to spread the risks of high cost care.

One employee comes down with a costly condition and premiums soar. Sometimes insurers try to get rid of the costly patient.

• **Administrative hassle.** Small employers don't have the time or expertise to search out the best insurance options, negotiate premium rates, administer health benefits, and handle consumer complaints.

A well-designed health insurance exchange would:

• **Improve the range of choices** for employees of small employers. An exchange would enable consumers to choose among multiple insurers, providers, and delivery systems offering standardized contracts.

• **Lower premium costs** for small businesses and individuals. An exchange would create a large pool and enable insurers to capture economies of scale and lower their administrative costs.

• Spread risks widely over thousands of people to make premium rates more **stable and predictable**.

• Reduce the burden on small employers **of administering health benefits**.

Most importantly, a well-designed exchange would be a **catalyst for innovation and improvement** in affordability, quality, and customer service resulting from healthy competition among both insurers and providers.

In order for a health insurance exchange to produce these beneficial results, it must have the following attributes:

• **Critical mass**. The exchange would need to act on behalf of a critical mass of people – at least 20 percent of the insured population that does not already receive Medicaid or Medicare. A large pool is needed to capture economies of scale, reduce insurers' administrative costs, and lower premiums. In addition, a pool of this size is needed to attract serious bids from insurers. To amass such a large purchasing pool, Congress might need to require all employers with fewer than 100 employees to join the pool. Alternatively, Congress could design incentives to join, such as providing premium subsidies only for those who participate in the exchange. An even stronger incentive would be to limit access to the tax exclusion to employees of employers who choose to have their employees participate in the exchange.

• **Protection against adverse selection into the exchange**. Most exchanges that have been tried in the past have failed. These failures were usually due to an adverse selection spiral — that is, higher-risk people enrolled in the exchange, which drove up premiums, which caused lower-risk people to drop out. This is a serious threat, especially when people can voluntarily join or not join the exchange. One way to deal with this is to make the

exchange the exclusive market for individuals and small groups. If use of the exchange is purely voluntary, however, there must be very strong mechanisms to minimize the likelihood of adverse selection.

• **Protection of insurers who enroll high-risk people in the exchange**. In any insurance market, there is a danger that high-cost people will tend to be concentrated in a particular insurer's plan. To protect these insurers, the exchange must have a "risk equalization" mechanism to compensate those plans for the higher costs of their enrollees. In addition, the use of a limited number of standardized, easy-to-compare benefit plans will lessen the danger of adverse selection into one of the insurers.

• **An active role**. Providing information to consumers about health plan choices is a basic function of an exchange, but it needs to take a more active role. The exchange should also have responsibility for:

- Designing decision-support tools for consumers.
- Providing a mechanism to collect and aggregate premium contributions from multiple sources (individual, employer[s], government subsidies).
- Establishing performance benchmarks for participating insurers, including provider network adequacy, benefit design, price, and quality outcomes.

• **Incentives to encourage healthy competition.** Ideally, health reform legislation would ensure that no subsidies for health insurance, whether provided by employers or the government, exceed the price submitted by the lowest-bidding qualified insurer and benefit package in the exchange. This feature would ensure that consumers would have a strong incentive to enroll in the plans that offer the best value for the money.

We know this will work. Exchanges already exist in our current health system, although we don't give them that label. The Federal Employees Health Benefit (FEHB) plan and the health benefit plans offered by some private employers have many of the features of an effective exchange, and it has successfully offered high-value health plan options for many years.

As comprehensive health reform legislation is crafted in Congress, it must have an effective health insurance exchange as a critical element. A large, robust exchange is essential for effective competition. A watered-down version of an exchange – too small, too weak, and vulnerable to adverse selection – will not offer significant benefits to individuals and small employers, and it will ultimately fail. An effective exchange will improve choices, lower costs, reduce administrative burdens, and help drive improvements in our health care system.

This entry was posted on Friday, July 31st, 2009 at 2:39 pm and is filed under Competition, Consumers, Health Reform, Insurance. You can follow any responses to

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August 12th, 2009 at 1:30 pm

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August 1st, 2009 at 10:07 am

Building a health marketplace that works / Health Affairs Blog « Three Fish Limit
July 31st, 2009 at 4:59 pm

6 Responses to "Building A Health Marketplace That Works"

mmchmbrs Says:
September 11th, 2009 at 10:30 am

This all sounds so complicated. I have been a nurse for 22 years. What I see are people that eat the wrong foods, are sedentary, smoke and drink to excess and have become debilitated as a result. The big killers are directly related to these risky behaviors – specifically, emphyzema, heart disease and diabetes. Diabetes causes it's own vast array of health problems. It is my belief that those people that choose not care for themselves and change risky behavior should pay for those choices. I am 51 years old and have no medical problems as I have always eaten a healthy diet even when I wanted to do otherwise, exercised and I do not smoke. Yet, I suffer the high cost of my insurance to pay for the poor choices of others. Marooyn Chambers, BSN, RN

Bob Stone Says:
August 24th, 2009 at 9:58 am

It appears that most commentators on the Health Reform Debate continue to focus almost solely on the financial issues. This is probably appropriate given that what is really being debated is coverage and payment reform. There is very little in any of the bills under consideration in either the House of the Senate that actually speaks to health and/or health care reform. The unfortunatel consequence of whatever "solution" might actually clear

Congress and be signed into law is that it will prove to be inadequate to address the health care cost issue — at least without some de facto price controls — becasue it will have failed to address the principal cause of escalating cost, namely the insatiable demand that is the inevitable by-product of building a system designed to treat illness, not to promote lifelong health.

James Mhyre Says:
August 18th, 2009 at 1:12 pm

I would suggest that the term “health marketplace” invokes two separate but interrelated markets, the health insurance marketplace and the health care marketplace. As a full time physician and occasional patient, I keep looking for economic reforms that encourage the patient and their physicians to choose conservative, less expensive options for care management. I will know that we have achieved health care marketplace reform when I see television advertisements from hospitals and other providers claiming to be the least expensive, not just the provider of superior quality and convenience, and cost will matter to me. As it is now, I do not know what the costs will be for just about any decision in my health care until after the fact, nor do I much care since it is mostly paid for by my insurance plan.

acavale Says:
August 8th, 2009 at 7:44 pm

This is the first time I have read anyone talk about the fallacies of the employer-based one-size-fits-all plans. It is not clear to me why this is not addressed more openly. Being a physician, a small business owner, employer and patient, I get to see all parts of the health insurance market. The main thing that has struck me many times is how unequal employer-based plans are – too much for younger/healthier employees, too skimpy for older-less healthier employees.

I would certainly welcome an exchange based on such principles, especially if it could simplify processes for potential patients/members and participating physicians. Other innovative ideas, such as options for patients and doctors to engage in tele-medicine and other types of medical interactions (with appropriate reimbursement) that allows care to be delivered/received without disruption of work or needing travel, should be encouraged. Currently all types of payers (govt and private) are least interested in offering such options.

Bill Stapleton Says:
August 5th, 2009 at 5:29 pm

We could easily create insurance exchanges today. If health insurance brokers could discount commissions, you would quickly see electronic exchanges with lower costs that reduce small group commissions which run as high as 6-8% of premium in many states.

Unfortunately it is against the law for brokers in the small group market (under 50 employees) to accept a lower commission than the insurance company dictates. Why would an employer go to an electronic exchange when he receives the services of a broker for "free."

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bett martinez Says:
August 4th, 2009 at 11:32 am

Cases for "reform" get laid out as logically as you like. Meanwhile reality happens. Here's a question quoted from editor of The Scientist:

An interesting story in The Washington Post today details the lobbying blitz being mounted by healthcare companies — including Big Pharma — surrounding the push to reform the country's healthcare system.

The Post story says that the industry is spending a staggering $1.4 million a day and employing the assistance of former legislators, ex-Congressional staffers, and other DC insiders to try and influence lawmakers central to the ongoing debate. While the article focuses on the ethical issues that attend hiring lobbyists so intimately knowledgeable of (read: cozy with) legislators and the internal workings of Congress, I can't help but wonder how the outlay of that kind of green affects the functioning of pharmaceutical companies.

Is the vast expenditure going to cause some slowdown in drug discovery/development? I'm sure Big Pharma companies can justify devoting so much money to lobbying Congress on the crucial issue of healthcare reform to their stakeholders, but what about the beneficiaries of pharmaceutical innovation? On balance, is the patient best served by Big Pharma lobbying or by Big Pharma bringing new drugs into existence and onto the market?

What do you think?

Bob Grant, Associate Editor – The Scientist

Attended a CME Conference for doctors and other health professionals last week, and one psychiatrist/professor from George Washington U echoed similar thoughts. Maybe the entire system needs an overhaul, a bypass, a transplant??

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